Ward, Robert Arthur

Notes on joint-stock companies

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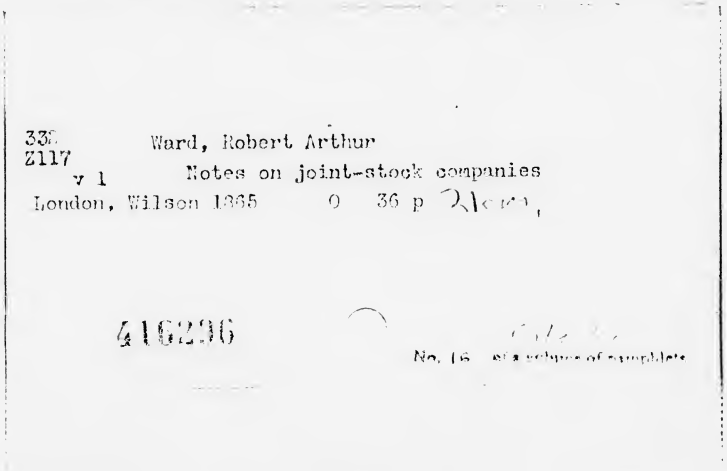

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NOTES

ON

JOINT-STOCK COMPANIES.

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NOTES

ON

JOINT-STOCK COMPANIES.

THIRTEEN years ago I published a Treatise on Investments, which was well received by the public, and favorably noticed in many metropolitan and provincial periodicals. Since that time a change has taken place in the character of the investments sought after by a numerous class of capitalists; the repeal of the law, which provided that any participation in the profits of an undertaking should entail a liability for all the losses incurred by it, to the extent of the whole fortune of every participator, has caused a very large number of projects to be brought before the public. The mania, which last year raged for speculation in the shares of joint-stock companies, was checked by the high rate of discount imposed by the Bank of England, and now that has fallen considerably, numerous fresh schemes, promoted under the Limited Liability Acts, are being frequently brought before the public. I have studied

the subject of investments generally for many years, and that of shares in joint-stock companies in particular, and I have had occasional glimpses of proceedings behind the scenes. I am not vain enough to fancy that my ideas will be of service to the few capitalists of intelligence, who, possessing information on the subject of their investments, make them with a fair degree of caution; but I do hope my suggestions may be of service to the many, who blunder hap-hazard into the first company offered to their notice, if it hold out promises of large returns for capital invested, without considering what hopes may be reasonably indulged, that the expectations, raised by the prospectus which has caught their attention, will be fulfilled.

It behoves those, who are about to subscribe for shares in any company, to consider well beforehand what will be the probable result of their operations; and it behoves those, who have already become shareholders, to watch with interest the proceedings of the companies in which they are interested, and to take an early opportunity of relieving themselves from their responsibilities, if they find the success of their company is doubtful, and they have no means of arresting its downward course. I do not mean from these observations to imply that it would be unwise and imprudent for persons to seek for no other investments than those which return a small income for the capital invested, though, as a rule, in such investments the capital is well secured. In

these days, when the cost of luxuries and necessaries has been increasing almost year by year, and will continue to increase, the income which, in the memory of those who are still young, sufficed for living in a style of comparative luxury, is now found to be insufficient for living in the same fashion: for these reasons, among others, prudent persons may and do legitimately seek to increase their incomes by becoming shareholders in joint-stock companies. Many such companies are no doubt got up simply and solely for the benefit of their promoters; others are stifled in their birth from want of capital sufficient to carry out feasible and well-considered projects; many others again are brought out in a flourishing manner and seem to command success; but they fail from want of management. There are, however, many which do succeed well, and year after year earn and pay dividends handsome enough to provide a considerable number of rich prizes to counterbalance the many blanks in the lottery of joint-stock speculation. Of late years the number of companies promoted has caused several solicitors to pay particular attention to this subject; and I should strongly recommend any person, proposing to run any considerable risk in subscribing to any joint-stock company to consult one of them. Their constant practice and unbiassed judgment will enable them to advise with discretion any clients, who may seek their assistance, and who will place before their advisers any special information, which may lie in

their power; the fees they will have to pay will be scarcely felt if the speculation they propose to enter into turn out a remunerative one; and if the charges paid to an adviser be the means of deterring a client from subscribing to a company unworthy of confidence, it will probably be the best invested money he has ever laid out. It must be in the experience of most persons that, when subscribing to any undertaking, their judgment and prudence are frequently biassed by their sanguine hopes of an immense return for their capital, and their steady disinclination and even incapacity to see any thing which may blight their prospects: such feelings as these are not partaken of by the solicitor, whose only desire, and, I may add, whose only interest, is to act in a manner best calculated to promote the objects of his client.

I am far from desiring to underrate the assistance that may be rendered by financial agents, some of whom I know to be highly honourable men, and well versed in the knowledge most useful in their profession; a member of the eminent firm of Chadwick, Adamson, M'Kenna, and Co., is one of my oldest and most valued friends; but solicitors have this great advantage over ordinary agents, that their communications with their clients are privileged, and this is a great benefit both to the client and the solicitor in discussing the merits of proposed companies, where sometimes a frankly expressed opinion of a company or some of its promoters may,

unless protected as a privileged communication, render its utterer open to the consequences of slander. Solicitors have also the advantage of a knowledge of the law; and if, not seeing their own true interests, they are inclined to sacrifice a client's welfare to their own, they would be severely punished by the courts of law, which recognize moral turpitude in a solicitor, while an ordinary agent transgressing in a similar manner would escape even from censure, if he kept without the pale of the criminal law.

Four conditions are necessary, in all cases, for the successful promotion and working of joint-stock companies: the scheme must be good in itself; it must be brought before the public at a seasonable time: it must have capital enough to carry it out; and it must be managed well. It is impossible to discuss individually the schemes of all the companies which have been recently floated, though I shall by and by make some remarks on the classes into which such schemes may be divided. Some are apparently of the wildest kind, even when their details are gathered only from the prospectuses that advocate them, and it is hard to see how such can be believed in by persons whose judgment is unwarped. There are other schemes, which, read only by the light of the prospectus, appear every thing which could be desired, but in which a slight investigation exposes many fallacies: the project of many companies is to purchase and carry on businesses theretofore con-

ducted by private individuals, and the suggestion to every one in this class is, if successful in the hands of a private person, why does he give it up to a company? Good answers no doubt may be rendered to this remark; a very large capital may be required; but, as a rule, a company as at present usually managed cannot compete successfully with an individual in a business which is within the means and capacity of the individual: the company must necessarily incur expenses which do not fall on the individual; and a man, who has been brought up to conduct a particular business, and whose daily bread depends upon his constant attention to it and proper supervision of it, has an immense advantage over a company, whose affairs are conducted by a board of gentlemen, possessing knowledge of the business more or less complete, and devoting only a small portion of their time to the conduct of it.

On the other hand, much may be said in favour of companies carrying on trades, and doing other business usually transacted by individuals. Such may prosper well if conducted by one well-paid and efficient manager, devoting his whole time to the business of his company, and thoroughly understanding it. He will know how to reap advantage from the numerous connexions which shareholders for their own interest would be ready to introduce, and if he succeeded in fairly earning a dividend of 10 per cent. per annum on the capital employed, he

might congratulate himself on the success of his efforts, though such a return by a private tradesman would hardly be considered satisfactory. I do not disguise the opinion I entertain of the very inefficient management usually obtained by a board of directors. Many gentlemen are directors of several companies at the same time, some of fifteen or twenty: they meet for an hour or two at each board, once or twice a week; frequently they omit several meetings altogether, so that an idea may be conceived by one set of gentlemen, the operations resulting from it commenced by another, and carried on by a third: but even if directors were all of them, as many of them undoubtedly are, anxious to do their best for the company they are interested in, it would be impossible to attend properly to several undertakings at the same time, each probably demanding a considerable amount of time and labour and a varied amount of information. Much better is it in my opinion that joint-stock undertakings should be managed by a well-paid and well-informed manager, answerable alone for the success or non-success of the undertaking so far at all events as it may be dependent on management, rather than to trust to a board of directors, a system which embraces all the evils of divided responsibility, without the safety that sometimes attends the deliberations of a multitude of counsellors. One or two shareholders might be nominated for the purpose of watching the operations of the manager, and of calling the general body of

shareholders together, if they thought it desirable to do so, but not to interfere in his operations, or to relieve him from any responsibility. All the shareholders might receive each month a report from the manager, and if he exhibited willingness to give any shareholder at all times information respecting the company, and occasionally met them at general meetings, he could hardly do much injury without their knowledge. But good management without undivided personal responsibility or without overwhelming personal interest is, depend upon it, very rarely attained.

In bringing a company before the public, it is desirable to have a board of directors, as the social status and position of each member of it frequently affords the chief, and sometimes the only, means of forming a judgment, whether the project is intended to be carried out in good faith, or is merely a bubble concocted for the benefit of some one behind the scenes; and even in this case I would rather see the board of directors before the company is floated take the title of promoters, and state how many shares each member has *bonâ fide* subscribed for: if the scheme be a good one, nothing will so well satisfy the public as to see a large number of shares subscribed for by gentlemen of position, who may be assumed to have made full enquiries into the probability of success, and to have had unusual facilities for doing so.

Much, very much, of the success of joint-stock

undertakings depends upon their management. It is within the experience of many, that companies with the fairest prospects, with a board of directors, to which no exception could be taken, and with ample capital, fail simply from mismanagement, or rather want of management at all. It is preposterous to suppose that a board of directors, few of whom attend regularly, and those few devoting only a few hours a week to the management of a gigantic concern, can, without the assistance of a very competent manager, prevent its drifting to ruin. The greatest possible care and circumspection should be exercised in selecting a person to manage the affairs of the company, whether under the supervision of the board of directors or not; and I strongly recommend that he should have a large personal interest in the affairs of the company. If he has merely a salary, which is the same whether the dividends are 20*l.* per cent. or nothing, his pecuniary interest in the company is limited to any few shares he may hold, and to his desire to keep the company afloat. He may do his duty, and no one may be able fairly to find fault with his conduct as manager, but, as a rule, he will transact the business in a very different manner from a man, who has a great interest at stake, whose salary is one commensurate with the responsibility entailed on him, as well as the knowledge and information he has to bestow, and the time he has to devote, or whose salary

may be largely increased by the success of the company.

Before taking shares in a company the following questions should be put to the secretary or promoters: 1. Who are the promoters of the company? 2. How many shares have been *bonâ fide* subscribed for, and by whom? State in your reply the number applied for by each person. 3. Are paid-up shares to be given to any director or other person? if so, state particulars and reasons. 4. Is any guarantee given to any subscriber against loss or liability? 5. Are any paid-up shares, and if so, how many to be allotted to the promoters of the company, and are they to receive any, and if any, what other advantages? 6. Is any remuneration, and if so, what, fixed for the services of the directors, manager, and officers of the company? 7. Are the whole amount of the shares to be allotted if applied for? 8. Are the allotments to be made in the order in which the applications are received, or at the caprice of the directors? 9. How are the directors, manager, and other officers removable? 10. Is it proposed to place any restriction upon the transfer of shares? 11. What is the qualification of a director?

If the project involves the purchase of property, inquire if the vendor is willing to receive any, and if any, how much of his purchase-money in paid-up shares, and whether the vendor subscribes for any shares, and if so, how many? Ask what are the

terms upon which the vendor sells; and inquire for full particulars of every transfer of the property during the last two years. If the project contemplates carrying on an established business, ask the reason of the vendor for desiring to give it up, and ask what have been the profits each year for the last four years, and by whom the profits have been ascertained, and whether by an examination of the books of the business, or how otherwise. Ask the secretary also a general question, if there be any other information within his knowledge which a person desiring to take shares ought to possess, to enable him to judge of the expediency of doing so. Some of these questions may not be applicable to the particular project into which inquiry is made, and the prospectus of the company may suggest others, and so probably will the replies received. The answers will, if truly given, throw much light upon the *bona fides* of the company. It is possible, no doubt, that false answers may mislead the inquirer; but if they do, he will be in a much better position as a shareholder, desiring to repudiate a position into which he has been misled, than if he had never made any inquiry at all: *Vigilantibus, non dormientibus, jura subveniunt.* In suggesting an inquiry about the remuneration of the promoters, I do not mean to insinuate that they are not to receive any consideration for their necessary expenses, exercise of ability, loss of time, and labour, and for the risk they incur; and I should look with very much

suspicion on any scheme, which proposed to give the promoters but an insignificant remuneration. I should conclude they intended to reap some advantage, which it was deemed expedient not to disclose. In asking for the particulars of every recent transfer of the property, the object is to see that the company is not got up merely to realize a profit on a purchase. Recently a considerable property and extensive works were purchased by a person, who formed a company, and sold his purchase to the company at a profit of about 100,000*l.*, an advance of something like 30 per cent. on the original purchase-money; such an operation as this necessarily involves one of two propositions, either the original vendor has sold his property for very much less than it is worth, or the company is asked to buy it at an exorbitant price. Every person proposing to accept shares in a joint-stock company should carefully peruse the articles of association; they will bind him as a shareholder, whether he signs them or not, the 26th section of the Companies' Act, 1862, enacting that the articles of association, when registered, shall bind the company and the members thereof to the same extent, as if each member had subscribed his name and affixed his seal thereto.

The Committee of the Stock Exchange are now happily doing their utmost to stop the operations of companies fraudulently concocted, and they refuse settling days to companies whose articles of association do not agree with their prospectuses; but as

the recognition of a company by the Stock Exchange is not necessary to the existence of a company, this rule will not relieve a shareholder from liability; though where the nature and objects of a company, as set forth in the prospectus, are altogether altered or materially extended by the articles of association, a shareholder unaware of the facts will be relieved from responsibility. (*Re The Scottish Universal Finance Bank, Limited; Ship's Case*, 12 *L. T. Rep. N. S.* 256; and *Kisch* v. *The Central Railway Company of Venezuela, Limited*, 12 *L. T. Rep. N. S.* 801.)

Persons subscribing for shares in the hope that if a winding up takes place they will have men of capital to share the liabilities with them may be mistaken; men of capital can transfer to men of straw, if the transfer be made without any secret trust, arrangement, or understanding, whereby an interest in the shares would be preserved and retained in the transferor; and this though the sole purpose of the transfer is to get rid of a liability for calls. In the case of *Reg. on the prosecution of Joseph Crea* v. *the Midland Counties and Shannon Junction Railway Company*, tried in the Court of Queen's Bench in Ireland (9 L. T. Rep. N. S. 151), Mr. Justice O'Brien, in delivering judgment, after laying down the principle above enunciated, and remarking that it was well settled, said, "With respect to a transaction of the kind being an unfair dealing towards the rest of the shareholders, I can

only say that the Act of Parliament gives the right of transfer, and every one who enters into these companies must know that he puts himself into the position, though he started with solvent fellow-shareholders, of being left with insolvent fellow-shareholders." And in this case a *mandamus* to register a transfer of shares was granted, although it appeared that the transfer, which however was a transfer out and out, not subject to any secret trust, for the transfer was made to a pauper, in order to enable the transferor to get rid of liability, and that the consideration money stated in the deed of transfer was a mere fiction. Mr. Justice Fitzgerald, it is true, entertained doubts about the propriety of the judgment, but merely on the ground that he questioned the expediency of permitting the exercise of the prerogative writ of *mandamus* to compel the Railway Company to act on a deed false on the face of it in a material particular, namely, the consideration and receipt for it; he did not doubt the correctness of the law as quoted above from the words of Mr. Justice O'Brien. Articles of association not unfrequently provide that shares should not be transferred without the consent of the directors, and this circumstance should have the consideration of a person proposing to subscribe.

Preference shares are often sought for by capitalists who desire a regular income without much risk of loss, and without, on the other hand, any chance of very large dividends. Persons purchasing

or subscribing for preference shares in companies registered under the Act of 1862, should examine beforehand the articles of association at the Joint-stock Companies' Registration Office in Serjeant's Inn, Fleet Street, London, to ascertain if the preference shares are created strictly in accordance with the terms of the articles. The 12th and 50th sections of the Companies' Act, 1862, give great powers to a general meeting of the company, authorizing it by special resolutions, passed as required by the 51st section, to alter the regulations of the company contained in the articles of association; but these powers do not extend to authorize the creation of preference shares, unless a power to do so is reserved in the original articles of association (*Hutton* v. *The Scarborough Cliff Hotel Company (Limited)*, 12 *L. T. Rep. N. S.* 289). Preference shares should, for the complete protection of the holders of them, be fully paid up shares; otherwise, in the case of a winding up, the holders may be put on the list of contributories.

Debentures in joint-stock companies are securities charging the property of the company with the payment of a certain sum of money on a given day, with interest thereon in the meantime at a fixed rate. Such securities are often sought after under the impression that they are to a great extent free from risk. This view is in many instances erroneous. When the articles of an association are silent on the subject, a joint-stock company has an implied power

to borrow money, and the Companies' Act, 1862, places no restriction on the amount which may be borrowed. Many companies are now seeking to borrow money on debentures for lengthened periods. It may happen that money lent on debentures is apparently well secured at the time it is lent; but it may be lost by circumstances over which the debenture holders have no control; for example, suppose a joint-stock company with a subscribed capital of 100,000*l.*, half of which is paid up, issue debentures to the extent of 10,000*l.* on January 1, 1865, payable seven years after date, a usual period, and on July 1, 1865, they issue fresh debentures amounting to 30,000*l.*, payable five years after date, and on January 1, 1866, borrow 20,000*l.* more on debentures, payable three years after date; the debentures issued first will be the most insecure of any, as their holders can do nothing to realize them until 1872, long before which other debentures will become payable, and the unpaid capital may be called up and spent in the meantime. Debentures should provide for their being immediately payable if other debentures are issued, or advertised for issue subsequently, and even then the holders must risk the loss of the unpaid capital and the property of the company before their debentures fall due. In companies formed by private Acts of Parliament, such as Railway Companies, there is generally a provision authorizing the company to raise a certain sum of money and no more, and bonds, issued for the purpose of raising money

beyond the amount the company is authorized to borrow, are illegal and cannot be recovered upon (*Chambers* v. *The Manchester and Milford Railway Company: Joint-stock Companies' Report, January*, 1865, *p.* 78). Bonds given to railway contractors, technically known as *Lloyd's bonds*, stand on a different footing, and are good securities, being merely treated as fixing a debt already incurred, and not as creating any fresh obligation (*White* v. *The Carmarthen and Cardiff Railway Company*, 33 *L. J.* 93 *Ch.* 9 *L. T. rep. N. S.* 439).

In the forthcoming edition of my work on Investments, I propose to enter more at large on the several different classes of joint stock-companies. At present I add a few remarks on them.

Shares in *Shipping Companies* are often lucrative investments, though the eight principal companies of that class, which have been established since 1861, have decreased in value; that is, the present value of their shares is less than the amount of their paid-up capital. The older companies as a rule are conspicuous for their success, especially the Peninsular and Oriental, and the Royal Mail Companies. In no class of joint-stock companies do bad management and ignorance give greater scope for ruinous losses. In any new shipping companies the prospect of a good trade in cargo and passengers should be well considered, and the necessity for running at a high rate of speed should be avoided unless subsidies or government grants can be obtained, or extra

freight charged; because a high rate of speed increases the consumption of coal and the liability of the machinery to destruction and injury.

Marine Insurance companies have been highly successful. Since the passing of the Limited Liability Act sixteen have been started; five have been comparatively unsuccessful, though only in a small degree. Two marine assurance societies have been eminently well managed, and consequently have been unusually successful: the Ocean Marine, and the Thames and Mersey. Each of these two companies has retained the services of an underwriter of eminence, thoroughly conversant with his business, at a salary of, I believe, 5000*l.* a year, and other advantages: the result shows the great success attending the retainer of a first-class official, even at a high scale of remuneration. The success of marine assurance societies depends mainly upon the skill, honesty, and ability of the underwriter or manager; if he insure unseaworthy vessels at A 1 rates, disastrous losses must inevitably ensue.

Life Assurance companies are among the least speculative of any, and are certain to yield large dividends, unless the cost of management, and the expense of obtaining business, bears too heavy a proportion to the business transacted. New offices, unless they have peculiar claims for public support, cannot compete with the many highly respectable older ones, without making sacrifices they cannot afford: they may appear to go on prosperously for

years, but the day of reckoning will come; for the first few years of the existence of a life assurance company the only claims it is called on to discharge are those which arise from persons insured with them dying prematurely.

Fire Insurance business incurs large risks, which can only be averaged when large business is transacted; and in this class of assurance, as in life assurance, there are so many old offices, that new ones can but rarely obtain business upon remunerative terms.

Land companies are as yet in their infancy. My impression is, that purchasing land with judgment and reselling it in lots with a registered title is a very desirable mode of investment, for a company or an individual; and it contains the element of speculation in a small degree only, as the land cannot be lost.

Nineteen companies may be classed under the head of *Engineering, Wagon, and Manufacturing companies*, with a paid-up aggregate capital of 2,729,000*l.* Four only have been comparatively unsuccessful.

Sixteen *Iron Work Companies*, with a paid-up capital of 3,590,000*l.* have shares whose market value is now considerably less than that amount; but some of these partake in some degree of the nature of mining undertakings, and are therefore unusually speculative: in almost all the cost of the necessary working plant, which is valueless for other purposes, is very great.

Under the head of *Tea and Plantation Companies*,

appear seventeen companies, with a paid-up capital of 1,159,500*l.*, worth now nearly 50 per cent. more. Assuming the price given for an estate is reasonable, the land well adapted for the purpose, facilities for transport good and cheap, and the management of the company unexceptionable, these companies merit attention.

Hotel Companies have enjoyed more favour from the public than almost any other class of joint-stock companies. The Great Western Hotel at Paddington was the first opened, and it has paid very large dividends, but very many circumstances combined to make this undertaking successful. Every hotel company professes to have some peculiar claim for public support, and each must stand upon its own merits. The management of hotel companies, including of course the management of the hotel, is very difficult; and in this, as in every other company, first-rate management is indispensable to success.

Joint-stock Banks have been the most successful joint-stock undertakings, as is evidenced by the high price of the shares of some of them. The chief source of profits to the joint-stock banks is the margin on the very large amount of deposits between the sum paid to the depositor, usually one per cent. less than the bank rate of discount for the time being, and the amount realized by using the deposits: and the larger the amount of deposits is in proportion to the amount of paid-up capital, the larger the dividend on such

capital will be; for example, if a bank has a paid-up capital of half a million and deposits of 14 millions, of which 12 millions only are used, and the rate of interest realized is the same as the bank rate of discount, the profits on the deposits yield a gross dividend on the paid-up capital of 24 per cent. per annum, without reckoning the interest derived from the paid-up capital itself, and without reckoning commissions, and other sources of income. But in my opinion the deposits are not unlikely to be considerably decreased, and there is a feeling beginning to prevail in many of the older banks, that the paid-up capital should bear a greater proportion to the deposits invested: both these causes will operate to decrease the dividends payable by joint-stock banks. While the rate of interest is high enough to permit the banks to pay 5*l.* per cent. for deposits, depositors are perhaps not anxious to remove them; but any continuance of a rate of discount which would only enable banks to pay 4*l.* per cent. per ann., or even less, to depositors, would induce them to look out for more remunerative investments. Financial companies and others are now offering 5*l.*, 6*l.*, and even 7*l.* per cent. per ann. for money deposited with them; and though investors should look with great care into the expediency of accepting such investments, the offers are likely to affect the deposits in banks considerably. The Bank of England may too, some day or other, offer interest for deposits, in which case the joint-stock banks could not fail

to suffer seriously from such a competition. Depositors may ask for some share in the profits arising from the use of their money; and though, on the other hand, means may be legitimately used to attract deposits that do not seem yet to have been adopted, I do not recommend investments in old-established joint-stock banks, at their present high prices; and there appears no opening at present for new undertakings of a similar character. Many of the old banks could not possibly pay all their deposits if a run, which an accident might cause, were to take place, though they might be perfectly solvent; and the necessity for closing the doors of a bank even for a day would probably bring down the shares to par, though there might be assets enough to pay the shareholders as well as the depositors 20*s.* in the pound.

Discount Companies realize their profits chiefly as banks do, by receiving deposits and using them at a profit; but with the exception of the National Discount Company, the value of their shares is less than the amount of the paid-up capital.

Financial Associations are companies of recent creation, which have held out hopes of very large dividends, and, in most instances, sorely disappointed their shareholders. They have published reports showing a profit of 30, 40, 50, and even cent. per cent. per annum on the paid-up capital. Their legitimate business is to assist contractors of large public works, and lend money on shipping

or securities which bankers do not care to take; but a large part of their business is to introduce new joint-stock companies to the public, receiving as a commission paid-up shares in those undertakings. Shares may be and are constantly sold and purchased at any given premium on the Stock Exchange, though there has been, in reality, no transfer or *bonâ fide* sale; and if they are quoted at the nominal value, so fictitiously created, it is easy to see that financial associations, crediting themselves with apparently valuable shares in the undertakings they have fostered, may publish very flourishing reports. If financial associations were very careful to bring before the public only such undertakings as appeared to command success, and were consequently ready to point to their offspring generally as examples of successful speculation, they themselves would, by raising their reputation, enhance the value of their shares, and increase the importance of their own position; but if company after company, promoted by any particular association, turn out a failure, the public will soon lose all confidence in the parent association, as well as in the companies it introduces.

As a shareholder may desire to become a director, I add a few words on the liability he will incur by doing so. Provisional directors on the committee engaged in the formation of a company before it is registered are liable for such expenses as they may actually incur by giving orders themselves; and each

director is almost always personally and wholly responsible for the orders given by himself jointly with his colleagues, though in the case of his being compelled by a creditor to pay debts, which others are liable for as well as himself, he may require them to repay him their proportion. And if certain gentlemen agree to act as provisional directors of a company, and appoint a secretary, they are liable to pay such expenses as he may incur on their behalf in bringing out the company, if acting apparently within the scope of his authority; this liability exists, even though there be an express agreement between the secretary and the provisional directors that all the preliminary expenses should be borne by such secretary, if such agreement be concealed from any person transacting business for such provisional directors on the orders of their secretary, though they may have been no parties to such concealment. (*Maddick* v. *Marshall*, 10 *L. T. Rep. N.S.* 272.) And the decision proceeds upon the very intelligible principle, that, where one of two innocent persons must suffer by the fraud of a third person, he ought to suffer who enabled the third person to commit the fraud.

Shareholders may sometimes desire to become directors, and they ought to know the penalties they may incur in that character. Whoever, being a director of a public company, shall concur in making, circulating, or publishing any written statement or account, which he shall know to be false in any material particular, with intent to deceive or defraud

any member, shareholder, or creditor, or with intent to induce any person to become a shareholder, or to entrust or advance any property to the company, or to enter into any security for the benefit thereof, shall be guilty of a misdemeanour, and liable to penal servitude for seven years or imprisonment for two years. (24 & 25 *Vict. cap.* 96, *sect.* 84.)

Every company registered under the Companies' Act is required to cause to be kept a register of its members containing the following particulars:—

1. The names, and addresses, and occupations, of the members of the company, with a statement of the shares held by each member, distinguishing each share by its number, and the amount paid or considered as paid on each share.
2. The date at which the name of any person was entered in the register as a member.
3. The date at which any person ceased to be a member.

For every day during which the company acts in contravention of this section it incurs a penalty of 5*l.*; and every director knowingly permitting such contravention incurs the like penalty. (*Companies' Act*, 1862, *sect.* 25.) By the 26th section an annual return of members is required to be made to the registrar of joint-stock companies on the fourteenth day succeeding the day of the ordinary general meeting (*sect.* 26). Every company making default in supplying such return incurs a penalty of 5*l.* per

day during which such default continues, and every director knowingly permitting such default incurs the like penalty (*sect.* 27). The register of members is to be open during business hours for inspection by any member gratis, and by any other person on payment of one shilling. Such member or other person may require a copy of the register, or any part of it, on payment of sixpence for every hundred words required to be copied. Every company refusing such inspection or copy incurs a penalty of 2*l.*, and in addition a penalty of 2*l.* a day during which such refusal continues, and every director knowingly permitting such refusal incurs the like penalty (*sect.* 32). Notice of any increase of capital, and where a company has not a capital divided into shares, notice of any increase of members must be given to the registrar within fifteen days, under a penalty on the company and every director knowingly and wilfully permitting the default of 5*l.* for every day during which such default continues (*sect.* 34). Every limited company should have its name painted or affixed on the outside of its office or place of business and engraven on its seal, and mentioned on all publications of the company, under a penalty of 5*l.* per day on the company, and the like penalty on every director knowingly permitting the omission; and, if any director authorizes the use of a seal for the company not so engraven, or authorize the issue of any notice, advertisement, or official publication of the company,

or authorize to be signed on behalf of the company any bill of exchange, promissory note, indorsement, cheque, order for money, or goods, bill of parcels, invoice, receipt, or letter of credit of the company, wherein its name is not mentioned as aforesaid, he shall be liable to a penalty of 50*l.*, and further, be personally liable to the holder of such bill, note, cheque, or order for the amount thereof, unless paid by the company (*sects.* 41 *and* 42). Every company is required to keep a register containing an entry of every mortgage and charge specifically affecting the property of the company; and every director is liable to a penalty of 50*l.* for a wilful omission to do so. Such register may be inspected by any creditor or shareholder of the company under a penalty of 5*l.*, and 2*l.* a day during which such inspection may be withheld, incurred by every director knowingly authorizing any refusal of such inspection (*sect.* 43). Every limited banking company, and every insurance company and deposit, provident, or benefit society, is required before commencing business, and on the first Monday in February and August to make a statement in the form marked D in the first schedule to the Act, and put it up in a conspicuous place in the office of the company, and every branch office, under a penalty of 5*l.* a day during which default is made in compliance with this provision, which penalty is payable by the company and by every director wilfully permitting such default (*sect.* 44). Every company

whose capital is not divided into shares is bound to send the registrar a list of directors, and a notice of any change under a penalty on the company and any director wilfully permitting such omission of 5*l*. a day each (*sects.* 45 *and* 46). A copy of any special resolution must be sent to the registrar within fifteen days after it is passed under a penalty on the company omitting to send it, and any director who may wilfully authorize the omission, of 2*l*. a day each. As however these penalties are not paid to the informer unless the justices or sheriffs before whom they are recovered specially so order (*sect.* 66), and as the manager of the company incurs similar penalties, they are very seldom enforced; nevertheless the responsibilities entailed by the Act on a director may make a nervous man unwilling to accept them by taking office.

These notes would scarcely be complete without an attempt to advise those, who unfortunately have accepted shares in undertakings, in which they have lost confidence. The first question for their determination is, whether they are willing to sacrifice their property in the undertaking for the sake of relieving themselves from responsibility. This will in a great measure depend on the amount of liability attaching to the shares: if the whole amount has been called up in a limited company, the liability is at an end, and the shareholder may do the best he can without reference to the contingency of loss; if a small amount on each share only is unpaid, it

may be worth while to risk a small amount of loss in the hope of avoiding a winding up, and of realizing something for the shares. And here I may remark that many companies are introduced to the public with shares of a considerable nominal amount, but coupled with a statement that a small call only will ever be required; this statement does not prevent a shareholder being obliged to pay every penny of the amount of the share, if it be wanted to discharge the obligation of the company: this, therefore, is a matter into which shareholders should look before embarking in such an association, and should consider when they contemplate the risk entailed by holding shares in such companies. Many of such associations are in fact companies with unlimited liability, and purposely so, for the fact of a large subscribed but unpaid capital necessarily adds to the credit and stability of the company. If a shareholder has reason to be dissatisfied with the affairs of the company in which he is interested, he should lose no time in acting, or seeing some good reason why he should be passive: he should seek the assistance of some person, able to advise with discretion and ability, and in seeking such advice he should detail every matter connected with the company, its formation and its operations, whether he thinks it important or not. In all cases of difficulty it is better to take the bull by the horns; and very many unfortunate shareholders in companies, which have been wound up would have saved themselves

from serious loss had they not permitted themselves to drift into trouble. If a shareholder desires to get rid of his shares at an early stage in the misfortunes of the company, he can probably induce some other shareholder, who is more sanguine than he, to buy them especially if such other shareholder has any peculiar interest in maintaining the company, or is desirous of avoiding an exposure, which a searching investigation might cause. By searching at the Joint-Stock Companies' office, in Serjeant's Inn, Fleet-street, a shareholder may obtain the names and addresses of his fellow-shareholders. If the shareholder cannot sell his shares except at a very alarming sacrifice, he had better act in unison with others as dissatisfied as himself; by uniting they will lessen their individual expenses, and add weight to their remonstrance to the directors, or their other operations.

The 56th section of the Companies' Act, 1862, enables the Board of Trade to appoint inspectors to examine into the affairs of any company under the Act, and to report thereon upon the application following, that is to say,—

1. In the case of a banking company divided into shares, upon the application of members holding not less than one-third part of the whole shares of the company for the time being issued.

2 In the case of any other company that has a capital divided into shares, upon the application of members holding not less than one-fifth part of the

whole shares of the company for the time being issued.

3. In the case of any company not having a capital divided into shares, upon the application of members being in number not less than one-fifth of the whole number of persons for the time being entered on the register of the company as members.

The application must be supported by such evidence as the Board of Trade may require for the purpose of showing that the applicants have good reason for requiring such investigation to be made, and that they are not actuated by malicious motives in instituting the same. The Board of Trade may also require the costs of the inquiry to be provided for. The inspectors have very full powers for conducting the examination; and when they report to the Board of Trade, a copy of the report can be obtained by the members upon whose application the inspection has been made. The Board of Trade may direct the cost of the enquiry to be paid out of the assets of the company. The company itself has power to appoint inspectors with similar powers; but the Board of Trade, it will be observed, may appoint inspectors at the request of a small minority of the shareholders.

If a shareholder has determined to sacrifice his shares for the sake of being relieved from the liability which the ownership of them entails, and this, though involving a sacrifice, is frequently the wisest course to adopt, the best thing to do is to

sell his shares for whatever they will fetch. If he does so *bonâ fide* the very day before the company is ordered to be wound up, he will escape much liability. The law is, that no past member shall be liable to contribute to the assets of the company, unless it appears to the court that the existing members are unable to satisfy the contributions required to be made by them in pursuance of the Act (*the Companies' Act*, 1862, *sect.* 38). And again, by another clause of the same section no past member shall be liable to contribute in respect of any debt or liability of the company contracted after the time at which he ceased to be a member. If a company keeps afloat for a year after a shareholder has parted with his shares, he escapes liability altogether, it being enacted by the 38th section of the Act that no past member shall be liable to contribute to the assets of the company, if he has ceased to be a member for a period of one year or upwards prior to the commencement of the winding-up. In order to constitute a valid sale of shares, so as to entitle the vendor to have his name excluded from the list of contributories, the transaction must be *bonâ fide*. There must be no reservation of interest to the vendor in the event of the company turning out better than was expected. A shareholder in a company *in extremis* is entitled to transfer his shares to any one absolutely, but a duly registered transfer to a trustee for the transferor, executed with the intention of getting rid of liability,

and reserving the benefit of the shares, does not relieve the transferor from his liability, even when the deed of settlement declares that trusts shall not be recognized, and that the person on the register shall be deemed the beneficial owner of the shares (*Chinnock's case, Re Athenæum Life Assurance Company*, 1 *Johns* 714); but it is not necessary that the purchaser should be a person capable of meeting the demands that may be made upon him in respect of the shares. (*Re the Phœnix Life Assurance Company, ex parte Hatton*, 31 *L. J. Chanc.* 340; 10 *W. R.* 313.)

In the case of the *Mexican and North American Mining Company, ex parte Hyam* (6 *Jur. N. S.* 181; 29 *L. J. Ch.* 243; 4 *De G. and J.* 544), a shareholder knowing the company to be in difficulties sold his shares to a warehousman in his employ a few days before an order for winding-up the company was obtained, the consideration being paid by the transferree out of the proceeds of certain shares assigned to him by the shareholder: it was held that there was no *bonâ fide* transfer, and that the shareholder was liable as a contributory. And in another case connected with the same company (*Ex parte Lund*, 27 *Bear*, 465; 28 *L. J. Ch.* 628), the Court held a transfer by a shareholder to his foreman inoperative, on the ground that it was not *bonâ fide*. On the other hand, in *De Pass's case, Re Mexican and South American Company* (2 *De G., F., and J.* 303; 30 *L. J. Ch.* 113), P. held 250

shares in a company, for which he had paid 1750*l.* A few days before the winding-up order, he being aware that the company was in difficulties, handed over the certificates to a clerk of his, there not having been any previous negotiation for the sale of them, and the clerk gave him 1*l.* for them. It was not disputed that P. made this transfer to escape liability, but the Court was satisfied on the evidence that it was an absolute and *bonâ fide* transfer out and out, without any trust or reservation, and the Court of Appeal held that P. was not a contributory. Where a company, therefore, is on the verge of bankruptcy, a shareholder may nevertheless shift a great part of his responsibility.

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ADDENDUM.

IT should be added to the observations at p. 26, that the mere circumstance of a person allowing his name to be published as a provisional committeeman of a projected joint-stock company does not confer on the secretary implied authority to pledge the credit of such person for work done on its account, or for goods supplied to the company. (*Reynell* v. *Lewis*, 15 *M. and W.*, 517. *Burbridge* v. *Morris*, 12 *L. T. Rep. N. S.* 426.) In the case of *Maddick* v. *Marshall*, mentioned in these notes, the provisional directors met and passed a resolution that the prospectus should be advertised, which was held to give the secretary an implied authority to employ an advertising agent for that purpose.

END OF
TITLE